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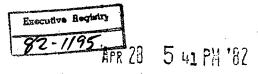
Ramarks:

Direct reply, please, with info this office.

Executive Secretary 28 April 1982

(10-31)

THE CHAIRMAN OF THE COUNCIL OF ECONOMIC ADVISERS WASHINGTON, D.C. 20006



April 28, 1982

MEMORANDUM FOR MARC LELAND, TREASURY

THOMAS B. CORMACK, CIA

L. PAUL BREMER, STATE

FROM:

ATI TIPE TO SEE THE SE

Jim Burnham

Subject:

Versailles paper on the Impact of the Oil Price Decline for Agency Clearance.

We would appreciate comments to Robert Murphy (395-5682) by c.o.b. Friday, April 30, 1982.

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Economic Impact of the Oil Price Decline

I. ISSUE

Lower oil prices will have a positive effect on economic performance in the major industrial countries. Estimates of the size of this effect depend crucially on whether the recent decline will continue in the future or be reversed. In addition, since oil prices are quoted in dollars, exchange rate movements will affect the magnitude of a given decline in price for countries other than the United States.

II. ESSENTIAL FACTS

Average official sales prices in international trade have declined by approximately one dollar per barrel over the past six months. Official sales prices do not, however, take into account special deals, credit arrangements, blending, etc., so that they probably understate the decline.

Spot market prices declined throughout 1981 and early 1982, but have firmed somewhat over the last few weeks. Over the past 6 months, Arabian light crude has gone from about \$35 a barrel to \$28 and back up to \$30.

A sustained 10 percent cut in oil prices would be expected to raise output in the OECD countries by half a percentage point, reduce the inflation rate in the near term by between one-half and one percentage point, and raise the current account surplus by \$10 billion. Because oil prices are quoted in dollars, the distribution of these benefits among OECD countries will depend on changes in the dollar exchange rates of these countries.

Several governments (Canada, France, Italy, and Japan) may try to prevent oil prices from falling because of an overriding desire to maintain pressure for conservation.

III. TALKING POINTS

Criticism: Falling oil prices will represent a set back for efforts in OECD countries to conserve energy and substitute other forms of energy for oil, unless taxes on oil products are adopted.

Response: Attempts to raise artificially the price of oil products through an energy tax will needlessly impose an obstacle to economic recovery. At present there is little reason to expect firms that have invested heavily in conservation measures to react to falling oil prices by shifting back to more oil intensive processes.

- 2 -

Criticism: As oil prices decline, OPEC surpluses will dwindle thereby reducing world saving and putting upward pressure on interest rates.

Response: Economic policies designed to reduce budget deficits, stimulate private saving, and spur productive investment can reduce the possibility that shrinking OPEC surpluses will actually reduce world saving. On the contrary, proper policies can help sustain a strong economic recovery without raising interest rates.

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DRAFTED BY:

BOB MURPHY

COUNCIL OF ECONOMIC ADVISERS

395-5682

CLEARANCES:

Central Intelligence Agency

Department of State Department of the Treasury